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SIPDIS

E.O. 12958: N/A

TAGS: [PGOV](#) [ECON](#) [IT](#) [ITALIAN](#) [POLITICS](#)

SUBJECT: NIGHT OF THE LONG KNIVES ITALIAN STYLE: FINANCE
MINISTER OUSTED

REF: A. ROME 2280

[1](#)B. ROME 0791

SUMMARY

[1](#)1. (C) FINANCE MINISTER GIULIO TREMONTI WAS FORCED OUT OF OFFICE JULY 2 BY DEPUTY PM FINI, WHO THREATENED TO QUIT THE GOVERNMENT ABSENT TREMONTI'S RESIGNATION. FINI'S PUSH FOR MORE POWER OVER ECONOMIC DECISION MAKING HAD BEEN STYMIED BY TREMONTI. BERLUSCONI, IN A SURPRISE MOVE, NAMED HIMSELF ACTING FINANCE MINISTER, A POST HE COULD HOLD UNTIL THE FY2005 BUDGET IS PASSED IN DECEMBER. AT BERLUSCONI'S JULY 5 ECOFIN DEBUT, ITALY SKIRTED AN "EARLY WARNING" FOR POSSIBLY EXCEEDING A KEY RATIO MEASURING THE BUDGET DEFICIT/GDP CEILINGS. THE GOVERNMENT NOW FACES TOUGH INTERNAL NEGOTIATIONS OVER ITS ECONOMIC PROGRAM, WITH BERLUSCONI RHETORICALLY COMMITTED TO SWEEPING TAX REFORM TO FULFILL HIS 2001 CAMPAIGN PLEDGE AND FINI'S NATIONAL ALLIANCE AND A CENTRIST COALITION ALLY LOOKING FOR AN UP TICK IN SOCIAL SPENDING FOR ITALY'S UNDERDEVELOPED SOUTH AND MORE PROGRESS TOWARDS FEDERALIZING ITALY'S GOVERNMENT AS CONDITIONS FOR CONTINUED SUPPORT OF THE COALITION. SPARKS WILL FLY AS BUDGET SEASON KICKS INTO HIGH GEAR, AND ESPECIALLY AS BERLUSCONI MUST REFEREE THE DIFFICULT POLITICAL CHOICES OF DECIDING WHICH SPENDING CUTS TO TAKE TO SATISFY COALITION PARTIES EAGER TO PROTECT THEIR OWN PORK BARREL INTERESTS. BERLUSCONI WILL ALSO PROBABLY NEED TO DODGE THE CRIES OF "FOUL!" AS HIS DETRACTORS WILL SEE HIS FINANCE MINISTER PORTFOLIO AS ONE MORE WAY TO SOLIDIFY HIS HOLD ON ITALY'S TELECOMMUNICATIONS SECTOR. END SUMMARY.

CENTER-RIGHT COALITION TENSIONS ERUPT; BERLUSCONI STEPS IN.

[1](#)2. (SBU) TENSIONS WITHIN THE CENTER-RIGHT COALITION OVER ECONOMIC POLICY CAME TO A HEAD JULY 2 WHEN DEPUTY PM FINI THREATENED TO WITHDRAW HIS NATIONAL ALLIANCE (AN) PARTY'S SUPPORT FOR THE GOVERNMENT UNLESS FM TREMONTI RESIGNED. PM BERLUSCONI, WEAKENED BY FORZA ITALIA'S POOR SHOWING IN LAST MONTH'S EURO-PARLIAMENTARY AND LOCAL ELECTIONS (REF A), WAS NOT IN A POSITION TO RESCUE TREMONTI, WHO DUTIFULLY SUBMITTED A RESIGNATION LETTER. THE HOSPITALIZATION OF NORTHERN LEAGUE LEADER AND STAUNCH TREMONTI ALLY UMBERTO BOSSI--INACTIVE IN POLITICS SINCE SUFFERING A STROKE THIS MARCH--CONTRIBUTED TO THE EX-FINANCE MINISTER'S VULNERABILITY.

[1](#)3. (SBU) EC COMMISSIONER MARIO MONTI IMMEDIATELY EMERGED IN ITALIAN NEWS REPORTS AS THE FAVORITE TO REPLACE TREMONTI. ACCORDING TO ANSA, ITALY'S LEADING WIRE SERVICE, BERLUSCONI SOUNDED OUT MONTI ON TAKING OVER THE FINANCE MINISTRY, BUT MONTI INDICATED A STRONG PREFERENCE FOR REMAINING IN BRUSSELS. SUBSEQUENTLY, BERLUSCONI SEIZED THE POWER VACUUM TO CLAIM THE FINANCE MINISTER POST FOR HIMSELF AD-INTERIM (NOTE: BERLUSCONI HAS PREVIOUS "DOUBLE HATTING" EXPERIENCE, IN HIS ROLE AS FOREIGN MINISTER FROM JANUARY-NOVEMBER 2002). APPEARING AT THE JULY 5 ECOFIN MEETING IN BRUSSELS TO DEFEND ITALY'S BUDGET DEFICIT REDUCTION PLAN, A BEAMING BERLUSCONI TOLD HIS FELLOW MINISTERS THAT HE LOVED HIS NEW JOB. ALTHOUGH PRESIDENT CIAMPI AND THE CENTRIST UNION FOR CHRISTIAN DEMOCRATS (UDC) HAVE SIGNALLED THEIR PREFERENCE FOR A SHORT INTERREGNUM, BERLUSCONI HAS NOT INDICATED HOW LONG HE WILL SERVE AS FINANCE MINISTER; PRESS REPORTS SUGGEST HE MIGHT HOLD THE POST UNTIL THE NATIONAL BUDGET LAW IS PASSED AT YEAREND. BERLUSCONI HAS AGREED TO THE CENTER-LEFT OPPOSITION'S CALL TO APPEAR BEFORE PARLIAMENT (HE IS SLATED TO ADDRESS THE SENATE ON JULY 14) TO JUSTIFY HIS DECISIONS AND EXPLAIN THE GOVERNMENT'S ECONOMIC PROGRAM.

TREMONTI PERFORMED WELL DURING ECONOMIC STAGNATION,
BUT NOT SYMPATHETIC TO PORK BARREL REQUESTS.

[1](#)4. (SBU) EVEN ACCORDING TO HIS DETRACTORS (THE PRO-SOCIAL SPENDING AN AND THE UDC), TREMONTI HAD COMPETENTLY MANAGED THIS PAST YEAR'S DIFFICULT ECONOMIC STAGNATION. HE ENSURED THERE WAS NO MAJOR SPENDING CUT THAT WOULD HAVE AGGRAVATED THE SLOWDOWN AND INSTEAD USED CREATIVE WAYS TO RAISE ADDITIONAL BUDGETARY REVENUES (I.E., ONE-TIME BUDGETARY MEASURES -- TAX AMNESTIES) TO TRY TO KEEP THE BUDGET DEFICIT MANAGEABLE. HOWEVER, THE AN AND UDC COMPLAINED HE DID NOT ACCOMMODATE THEIR (PORK BARREL) INTERESTS (MAINLY FOR SOCIAL SPENDING IN THE IMPOVERISHED SOUTH), NOR DID HE HELP FINANCE THE NORTHERN LEAGUE'S PET PROJECT TO FEDERALIZE ITALY'S

GOVERNMENT.

BUDGETARY PROBLEMS: POLITICAL PRESSURE FOR TAX CUTS

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LEADERSHIP OF THE FORZA
ITALIA BY PRESSING FOR HIS PET 2001 CAMPAIGN PROMISE --
LOWERING PERSONAL INCOME TAXES AND COLLAPSING THE PRESENT
FIVE BRACKETS.

16. (C) COMMENT: BERLUSCONI MIGHT BE BETTER PLACED TO
IMPLEMENT TAX CUTS, WITH THE AXING OF BUDGET-HAWK TREMONTI.
HOWEVER, BERLUSCONI MUST CONSIDER THE EFFECT SUCH REFORM
WOULD HAVE BOTH IN ITALY, AND WITHIN THE EUROPEAN MONETARY
UNION (EMU): IN ITALY, LOWER TAXES WOULD MEAN A SHORT-TERM
REVENUE LOSS TO THE ALREADY-MALIGNED BUDGET -- AND THUS MORE
PRESSURE ON THE BUDGET. HE WOULD ALSO HAVE TO DEFEND AGAINST
POLITICAL CHARGES STEMMING FROM ANY TAX PLAN THAT APPEARED TO
FAVOR WEALTHY TAXPAYERS.

17. (C) AS FOR THE EMU, THE NEW FINANCE MINISTER MUST CONTINUE
TO STEER ITALY CLEAR OF A EUROPEAN COMMISSION "EARLY
WARNING" ON BUDGETARY EXCESS. SPECIFICALLY HE MUST STEER
ITALY'S BUDGET JUST BENEATH THE EU CEILING OF A DEFICIT/GDP
RATIO OF THREE PERCENT AND SHOW CREDIBLE PROGRESS ON LOWERING
ITALY'S HOPPING DEBT STOCK (106 PERCENT OF GDP). HE MUST
ALSO MAKE THE DIFFICULT POLITICAL CHOICES TO DECIDE WHICH
SPENDING CUTS TO TAKE TO SATISFY FRACTIONAL COALITION PARTIES
EAGER TO PROTECT THEIR OWN PORK BARREL INTERESTS. END
COMMENT.

IMPLICATIONS FOR INTERNATIONAL CREDITWORTHINESS

18. (SBU) THE INTERNAL COALITION DEBATE ABOUT THE FINANCE
PORTFOLIO HAS BECOME VERY PUBLIC. BOTH THE EU COMMISSION AND
INTERNATIONAL RATING AGENCIES WILL CERTAINLY BE MONITORING
PUBLIC STATEMENTS AS INDICATIVE OF THE GOVERNMENT'S POLITICAL
WILL TO TAKE THE NECESSARY PAINFUL STEPS. ITALY CANNOT
AFFORD A LOWERING OF ITS CREDITWORTHINESS ON INTERNATIONAL
MARKETS.

IMPLICATIONS FOR ELECOMMUNICATIONS SECTOR

19. (SBU) AN ADDITIONAL ISSUE SERVED BY THE PM'S ASSUMPTION OF
THE FINANCE PORTFOLIO CONCERNS THE CONFLICT OF INTEREST
CHARGES THAT DOG BERLUSCONI IN THE TELECOMMUNICATIONS SECTOR.
IN HIS PRIVATE LIFE, THE PM IS ALSO OWNER OF THE LARGEST
PRIVATE-SECTOR MEDIA NETWORK IN ITALY (MEDIASET). SINCE THE
BEGINNING OF THIS GOVERNMENT IN 2001, HE HAS BEEN SCATHED IN
THE PRESS AND BY OTHERS OUTSIDE THE COALITION WITH CHARGES OF
A CONFLICT OF INTEREST BETWEEN HIS ROLE AS PM AND AS
MEDIASET'S LARGEST SHAREHOLDER. HE HAS MANAGED TO DEFLECT
THESE CHARGES OF CONFLICT OF INTEREST, BUT THEY MAY BE MORE
DIFFICULT TO REBUT WITH HIS NEW FINANCE MINISTER POWERS.
SINCE THE GOI OWNS 100 PERCENT OF THE STATE-TELEVISION
NETWORK (RAI), WHICH IS ALSO UNDER THE CONTROL OF THE FINANCE
MINISTER, THERE IS ON PAPER AT LEAST STRONGER GROUNDS FOR
MORE STRIDENT ACCUSATIONS OF CONFLICT OF INTEREST.

NEXT STEPS

10. (SBU) WITHIN ABOUT TEN DAYS, THE CABINET MUST APPROVE BY
DECREE-LAW THE DEFICIT REDUCTION PACKAGE UNDER DISCUSSION.
THIS WILL BE FOLLOWED BY THE PREPARATION AND APPROVAL OF THE
2005-2008 DPEF (DOCUMENTO DI PROGRAMMAZIONE ECONOMICA E
FINANZIARIA), A FOUR-YEAR ECONOMIC PLAN THAT SETS FORTH
ECONOMIC/BUDGETARY GOALS FOR EACH YEAR THROUGH 2008.

COMMENT

11. (C) BY DETHRONING TREMONTI, DPM FINI AND HIS NATIONAL
ALLIANCE PARTY ACHIEVED AN IMPORTANT SYMBOLIC VICTORY. FINI
WANTS THE GOVERNMENT TO DIRECT ADDITIONAL FUNDS FOR PUBLIC
WORKS TO ITALY'S UNDERDEVELOPED SOUTH, AN IMPORTANT AN
ELECTORAL BASE, AND HIS LONG-STANDING STRUGGLE TO OBTAIN MORE
POWER OVER ECONOMIC DECISION MAKING HAD BEEN EFFECTIVELY
BLOCKED BY TREMONTI. FINI APPARENTLY WAS TAKEN BY SURPRISE
BY BERLUSCONI'S DECISION TO REPLACE TREMONTI WITH NONE OTHER
THAN HIMSELF, BUT HAS ADOPTED A WAIT-AND-SEE APPROACH IN THE
HOPES THAT HIS STURDY--IF NOT ALWAYS WARM AND
FUZZY--RELATIONSHIP WITH THE PM WILL FOSTER THE ELUSIVE
COALITION COLLEGIALITY HE HAS BEEN SEEKING (REF B).

12. (C) FOR BERLUSCONI, REMOVING THE ABRASIVE TREMONTI WAS A
CALCULATED RISK THAT A MORE PRODUCTIVE POLICY DIALOGUE COULD
DEVELOP AMONG THE COALITION'S LEADING PROTAGONISTS.
NEVERTHELESS, IF SPECULATION IN THE ITALIAN PRESS THAT

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N THE TELECOMMUNICATIONS

SECTOR HE ALREADY DOMINATES TURNS OUT TO BE TRUE, TENSIONS COULD BOIL TO THE SURFACE AGAIN THIS YEAR. BOTH THE AN AND THE MODERATE UDC WILL HAVE DIFFICULTY SWALLOWING AN ECONOMIC PACKAGE THAT SIMPLY RECAPITULATES INITIATIVES LONG CHAMPIONED BY TREMONTI, INCLUDING TAX REFORM THAT FAVORS THE WEALTHY. MOREOVER, WHILE FOR NOW THE NORTHERN LEAGUE IS FULLY BACKING BERLUSCONI'S INTERIM TERM AS FINANCE MINISTER, IT TOO HAS THREATENED--HARDLY FOR THE FIRST TIME--TO BOLT THE GOVERNMENT IF COALITION LEADERSHIP DOES NOT RENEW ITS COMMITMENT TO DEVOLVE POWERS TO ITALY'S REGIONS.

13. (SBU) IS THIS THE USUAL STUFF OF ITALIAN POLITICAL THEATER? WE CONTINUE TO THINK THE ANSWER IS YES, PRIMARILY BECAUSE, AFTER TREMONTI'S DEMISE, WE SEE LITTLE UPSIDE FOR ANY OF THE COALITION PARTNERS TO LEAVE A GOVERNMENT THAT OFFERS THE ONLY AVAILABLE MECHANISM FOR THEM TO ACHIEVE THEIR POLITICAL AND POLICY GOALS.

14. (SBU) IN ALL OF THIS, HOWEVER, THE GOI MUST NOT TREAT LIGHTLY THE EMU'S INTENT TO REIN IN ITALY'S BUDGETARY EXCESSES. ECONOMIC OBSERVERS ALSO DO NOT SEE ANY MORE OBVIOUS CREATIVE WAYS (I.E., OTHER ONE-TIME MEASURES LIKE THIS YEAR'S TAX AMNESTY) THAT THE NEW FINANCE MINISTER COULD USE TO SHORE UP THE GOVERNMENT'S BUDGET, WHILE ITALY CROSSES ITS FINGERS AND WAITS FOR ECONOMIC GROWTH AND A TURN AROUND IN THE ECONOMY. END COMMENT.

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